

Getting signed up –
energy services in the public sector

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Acknowledgments

This Guide has been produced to assist public sector organisations in the development and procurement of energy services contracts. The Guide aims to explain the complex issues associated with such contracts and hence reduce the barriers to their uptake.

In this way it is hoped to stimulate energy services market growth and thus increase the total investment in energy efficiency measures. This will in turn lead to a reduction in CO₂ emissions and assist in meeting government targets for climate change.

The Guide is designed for management and project development staff, breaking down the process into a number of stages with two levels of detail.

Managers can get an overview of energy services contracts from the process descriptions.

Project development staff can get the same information, but can also follow up with more details for a better understanding of each process stage.

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Overview Energy services – the business proposition

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1.1 What are energy services contracts?

The term energy services contract (ESC) describes arrangements by which an organisation may contract out the provision of its energy services to an energy services company (ESCO) (see section 1.3).

The agreements provide a means by which an organisation can transfer the responsibility of ensuring cost-effective procurement, security of supply and meeting end-user needs.

This transfer of responsibility generally requires that services to be delivered through such contracts are specified in terms of required outputs rather than by specifying the means of delivery.

For example, the contract may specify the energy provision in terms of that which is required to maintain a process or to ensure that a satisfactory working environment is achieved.

This approach differentiates ESC from more traditional forms of energy procurement.

In order to meet the contract demands, ensuring efficiency and continuity of supply throughout the term, it will often be necessary for the ESCO to invest in new plant and equipment. Such investments may involve significant capital and typically take place at the beginning of the contract period. The need for immediate capital is often a key incentive for procurers to seek such contracts. Depending on the allocation of risks, energy services agreements may involve a public private partnership, such as the Private Finance Initiative (PFI), and may also be part of much larger schemes.

Further information on PFI can be obtained from: Partnerships UK, Private Finance Projects Team – tel 020 7270 4623; Office of Government Commerce, Private Finance Policy Team – tel 020 7389 9739; or Public Private Partnerships Programme (4Ps) – tel 020 7472 1550

1.2 What are the benefits of energy services contracts?

The benefits to be obtained from ESC include the following.

Providing capital funding

A specialist contractor can provide immediate funding for the replacement of outdated equipment or the installation of new systems. This allows public funds to be used for core activities rather than investing in energy plant. This type of private sector investment might be part of a Public Private Partnerships (PPP) arrangement.

Transferring risk

By accepting responsibility for investment and staffing, and underwriting the performance of site services, a specialist contractor takes on risk, such as project over-run and over-spend, that the public sector would otherwise bear. The extent of risk transfer is both flexible and negotiable.

Taking a long-term view

A long-term partnership provides the contractor with the incentive to invest for optimum savings, taking account of payback periods, affordability and the sharing of benefits between both partners. This also stimulates continuing investment in plant during the contract.

Improved budgeting and cost control

The life-cycle costs are known by the client at the start of the contract. This facilitates improved long-term planning and budgeting. Revenue payments can be structured to meet cash flow requirements within the year.

Reducing energy costs

A specialist contractor can assess how energy savings can be achieved and develop the most appropriate and energy-efficient solution. The contractor can also negotiate fuel purchase strategies tailored to individual sites. These can be more cost-effective, flexible and appropriate than central fuel purchasing.

Freeing management resources

A specialist contractor will take care of all day-to-day plant operation and maintenance activities. This releases the client's management and staff to concentrate on the organisation's core activities and focus on strategic energy issues.

Managing environmental and health and safety matters

Through managing design, operation and maintenance activities, contractors can take on many of the duties of complying with environmental targets or legislation, and will be responsible for potential risks such as emissions, spillages, and hazards.

1.3 What is an energy services company (ESCO)?

The contracting out of energy-related activities is not new. Examples such as contract energy management and facilities management have been common for many years. Traditionally, the companies that provided these services were subsidiaries of energy supply companies, who sought to offer additional value-for-money services for their customers. The market has now evolved to include independent energy services companies. For larger or more diverse projects, the ESCO may be a joint venture (perhaps including a public sector organisation in partnership with others).

1.4 What types of energy services contracts are there?

An energy services agreement may be tailored to accommodate specific client needs and achieve best value for money. In its simplest form, this may be the provision of an energy management service. A wider service may include project funding, energy supply, operation and maintenance and energy management.

In the most comprehensive form, the contract may be based on a DBFO (design, build, finance and operate) arrangement. These arrangements incorporate the following features.

- The ESCO provides the design and installation of any new energy-efficient plant required.
- The ESCO provides finance for the construction of new energy plant, and/or refurbishment and improvement of existing plant.
- When construction is completed, the ESCO operates and maintains the facility for an agreed period.
- The ESCO negotiates and arranges the competitive supply of fuel and power and sells usable energy on to the client. There may be an element of risk-sharing on energy prices.

- The ESCO provides on-site energy management and control to meet specified energy or environmental performance targets.
- At the end of the contract, the energy plant ownership may be transferred to the client or made available to a new service provider (ie the contract could include a purchase option and a formula to derive an agreed residual value). Such contracts are sometimes referred to as BOOT (build, own, operate and transfer) contracts.

In return for the provision of these services, the ESCO recovers the cost of its capital investments and operation through variable and/or fixed charges. The charges reflect the term of the proposed contract and the extent to which risks are transferred to the ESCO. Payments to the ESCO normally commence once construction is complete and the service is available.

Where significant capital investment is involved on the part of the ESCO, the contract will generally be long term. This enables the ESCO to recover its investment, while at the same time providing a saving for the client. For a large investment project, a term of 10 years is not unusual and it may be as long as 25 years (depending on the scale of investment and its impact on affordability).

As mentioned above, energy services agreements can be tailored to suit specific circumstances.

It may be desirable for an ESCO to purchase the client's existing energy plant, upgrade and refurbish it, and utilise it to fulfil the ESC. The ESCO's investment is recovered in a similar manner to that mentioned above. These arrangements are often generically referred to as ROL (rehabilitate, operate and leaseback) contracts.

Usually, it is desirable to transfer all operational responsibility to the ESCO. Occasionally, it may be beneficial for a client to retain some operational management of the plant. Typically, this might be where specialist expertise is retained and best provided by the client for strategic or safety reasons. Where there is an element of such partnership management, the arrangements are often generically referred to as BOP (build, operate and partnership manage) contracts.

In order to improve the cost-effectiveness of energy purchase for the client, it may be desirable to introduce increased flexibility to the energy supply arrangements. Such schemes might allow the client to obtain energy from an alternative source to the ESCO plant, subject to competitive pricing tests, and the ESCO to sell surplus energy from its plant to third parties outside the energy services agreement.

Overview

Energy services – the strategic issues

2

This section describes the principal processes and factors that should be considered when selecting an ESC, together with guidance on the procurement routes that should be followed.

2.1 Establishing the requirements for energy development and scope of supply

Before embarking on the process of energy services development, it is important to consider all aspects and deficiencies of the current provision and establish how changes may be of benefit to the organisation's long-term strategic objectives. Detailed consideration at this stage will ensure that opportunities are not missed later. The need or opportunity to 'do something' about energy may arise for a variety of reasons:

- the need for plant replacement or refurbishment
- excessive energy consumption and cost
- excessive operational costs
- the requirement to meet energy efficiency and environmental targets
- the poor quality of existing services
- changing operational requirements or organisational restraints
- the expiry of existing contracts
- changes in regulatory responsibilities
- changes to the energy demand patterns.

An ESC may provide a procurement option that meets the organisation's strategic needs for energy development. If best value for money is to be obtained, the scope must be both realistic and practical. It is appropriate at this stage to hold preliminary discussions with ESCOs to establish the role that an ESC could play, and thus its likely scope.

These considerations are developed as follows.

2.2 Creating the project team

The process of developing an ESC, whether it falls within the PFI category or not, will be demanding of management time and expertise.

If your organisation is to secure value for money, you will need to establish the commercial opportunities presented by the energy development requirements and convey these to the potential ESCO bidders. It will be necessary for you to consider simultaneously various innovative responses from ESCOs.

To ensure that ESCOs are convinced of your organisation's commitment to the project, it is important from the outset to establish an implementation programme and evaluation criterion, which must be adhered to.

Once the process is underway you will find that much management time is spent defining detailed requirements and ensuring that your organisation's interests are safeguarded.

With this in mind you should, in forming the project team, decide which of your organisation's management team is competent and authorised to deal on its behalf and what external expert support is required. The team will need to be multi-disciplinary and include representatives of all those who have an interest in the project outcome.

It is probable that much of the detailed process for developing an ESC will be new to your organisation's management and it is suggested that the following professional advisers be considered when setting up the project team.

Financial

You will probably benefit from the advice of someone who can demonstrate how to structure the requirements to achieve best value for money and an affordable solution. This will be particularly important if the project falls within the PFI category. Such advice may include a full appraisal of values, negotiating elements and ESCO financing structures.

Legal

It is probable that, for any ESC involving capital investment by the ESCO, your organisation will be contractually committed for a significant period. It is, therefore, recommended that legal advice be sought at the earliest opportunity to ensure its interests are protected. Seeking legal advice early will mean that the advisers are able to gain a sound understanding of the organisation's requirements.

Technical

While it is possible that technical expertise exists within your organisation's own management team, external advice may be useful to assist in evaluating innovative schemes put forward by ESCOs. Again, an early involvement is useful.

Procurement

Procurement expertise is vital to ensure that any contract is soundly based and let in accordance with the appropriate regulatory framework.

Human resources

Staffing implications need to be considered, particularly if the in-house staff are to transfer to a new ESCO.

When appointing external advisers, you should look for firms that have knowledge of ESCs/PFI and a track record of providing practical advice which can assist the team's assessment of risk.

It is also advisable to consider, early on, the essential contract management arrangements – ie what will be the critical success factors several years on, how will these be measured and who will do it.

2.3 The appropriate transfer of risk

The transfer of risk from the client to the contractor is an important aspect of contracting for energy services. However, this does not mean that all risks should be transferred. Risk should be allocated to the party best able to manage the risk and at least cost, in order to ensure improved value for money.

When you are transferring risk, the ESCO is accepting responsibility for which it will require due reward. The greater the transfer of risks the greater the reward and consequent cost to your organisation. It is, therefore, important to transfer only risks that are appropriate. For PFI contracts it is important, however, that sufficient risks are transferred to ensure that the accounting requirements for off balance sheet treatment of the transaction are met.

To secure appropriate risk transfer which will result in value for money, it is necessary to ensure that the scope of a contract is sufficiently widely drawn. If the ESCO has clear ownership and responsibility it will be able to accept and manage associated risks accordingly. If the client seeks to retain an element of control or operational responsibility, and yet still seeks to transfer risk, the ESCO will increase the price. In comparing options to establish value for money, it will be important to place a financial value on each of these risks.

The following table identifies categories of risks that need to be allocated and gives illustrative examples within each category.

Category	Examples
Design and construction	<ul style="list-style-type: none"> ● Failure to meet specified requirement. ● Capital overspend.
Project over-run	<ul style="list-style-type: none"> ● Failure to deliver service on time.
Project financing	<ul style="list-style-type: none"> ● Ability to raise finance. ● Cost of raising finance.
Operation	<ul style="list-style-type: none"> ● Increased operating cost. ● Poor quality or availability of service. ● Inadequate maintenance.
Regulatory or legislation	<ul style="list-style-type: none"> ● Changes in statutory requirements. ● Planning permission.
Residual value	<ul style="list-style-type: none"> ● Value of asset at end of contract.
Technology or obsolescence risk	<ul style="list-style-type: none"> ● Asset may become less appropriate over project life.
Service demand	<ul style="list-style-type: none"> ● Changes in peak demand. ● Changes in usage.

2.4 Establishing employee-related issues

Further policy guidance on TUPE can be found in the Cabinet Office guide: 'Staff transfers in the public sector – Statement of Practice' (January 2000). The statement also covers the position regarding pensions, which are not included within TUPE. The guide can be found on the Cabinet Office website at: <http://www.cabinet-office.gov.uk/civilservice/2000/tupe/>

Awarding a contract for the provision of energy services to an ESCO has implications for employees of the public employer who were previously employed to provide those services.

The operation and maintenance of energy plant may typically be provided under an ESC. Such an agreement may reduce or obviate the need for the existing public sector employees.

This may have directly beneficial consequences in that these staff may be freed to provide a valuable labour resource elsewhere within the client's organisation. There may also be redundancy implications although this should be unlikely as the staff might be transferred to the employment of the ESCO under the contract. Transfer issues are addressed by the Transfer of Undertakings (Protection of Employment) regulations (TUPE). The TUPE regulations generally apply where there is a stable economic entity before transfer that retains its identity after transfer (ie business as usual).

It is essential that the public sector organisation makes the necessary employment policy decisions prior to developing a strategy, taking legal advice regarding staffing and TUPE issues, as well. This must not wait until near the end of any tendering process, but be built in at the beginning.

The protection offered by TUPE operates at two levels.

At the individual level, employment protection is given both in respect of the continuation of terms and conditions of employment in any new employment for those who transfer, and also in respect of any loss of employment for transfer-related reasons (whether at the hands of the new or former employer).

At a collective level, the protection of employees affected by transfers is effected firstly by giving employee representatives the right to be informed and consulted about transfers subject to TUPE, and secondly by providing for the continuation of any relevant collective agreements reached with the former employer, in the new employment situation.

Therefore, where an energy services agreement will result in the transfer of staff, full consultation must be provided.

2.5 The implications of acquiring capital assets through energy services contracts

It is often desirable that the contractor invests in new plant to fulfil the service requirements. Understanding the fiscal treatment of this investment and the effect it will have on the organisation's capital and revenue budgets is important.

Further information can be obtained from: HM Treasury Technical Note 1 'How to Account for PFI Transactions' (revised June 1999)

The accountancy treatment of investments made under this type of contract is subject to the provisions of Financial Reporting Standard 5 (FRS5) 'Reporting the Substance of Transactions' and Statement of Standard Accounting Practice 21 (SSAP21) 'Accounting for Leases and Hire Purchase Contracts'.

Where the project can essentially be defined as the provision of a service, and the risks associated with the property sit predominantly with the ESCO, the assets will not need to be accounted for on the public sector balance sheet.

If the project cannot be viewed simply as a service, retains an element of identifiable capital expenditure and it is clear that the underlying risks attaching to the property belong to the client, then this will be treated as an on balance sheet project in the conventional way. An organisation's capital budget may be reduced accordingly and capital charges will apply.

Regardless of the fiscal treatment, all expenditure on acquisitions should demonstrate value for money.

Further information on PFI credits can be obtained from: Public Private Partnership Programme (4Ps) – tel 020 7472 1550

Where a local authority is the client, a scheme may receive support as a PFI project through a PFI credit, which attracts revenue support. Local authority PFI schemes must satisfy project criteria set by the relevant government department responsible for the scheme. This is most likely to be the Department of the Environment, Transport and the Regions or the Department for Education and Employment. An outline business case for the scheme will need to be submitted with the application to the relevant government department.

2.6 Understanding the various means of procurement

For the public sector, there are two principal procurement routes that will be relevant for ESCs – traditional procurement and PPP/PFI procurement. Which of these is appropriate will depend on the scale and scope of the intended project.

Traditional procurement

These procedures will usually be appropriate when the analysis of best value for money shows that any capital investment requirements should be provided by the public sector. These projects will usually be straightforward with input and output requirements easily defined. Typically, they will be projects that do not offer significant opportunities for risk transfer to the private sector. Under these circumstances, a conventional competitive tendering exercise will suffice (receipt of sealed bids for the provision of services to a detailed specification). The most economically advantageous bid (which may take into account a number of factors beyond simple cost) will be used to select the contractor.

The procurer's management effort required should be relatively small and restricted to the essential preliminaries of:

- preparing a business case
- appraising the options
- writing a specification
- posting the relevant advertisements.

PPP/PFI procurement

Alternatively, best value for money may be offered by a PPP with private capital investment. The improved value for money will generally derive from allocating risks to the party best placed to manage them.

These are likely to be complex projects, with scope for the contractor to offer innovative solutions for efficient energy supply and management, and involving significant private capital investment.

The scope for adding value through innovation together with the transfer of associated risks is best achieved by negotiation, and the use of the negotiated procedure facilitates this. The negotiated procedure is permissible where the service requirement cannot be readily defined and therefore where an output specification (see section 4) is to be employed. A contractor will have greater scope to come up with an innovative solution where the required service standards or outputs are specified rather than the means of achievement.

OJEC requirements

Whichever procurement route is appropriate, it will be necessary to observe EU rules on the procurement of assets and services. In the context of ESCs, EU rules require that all projects exceeding published threshold values be advertised in the Official Journal of the European Community (OJEC).

It is worth considering at this point that the scope of a project could change during negotiation (if that is the route), thus, while its value may initially appear to be below the threshold, it could subsequently exceed it, resulting in a loss of time through necessary re-advertisement.

Examples of advertisements and drafting notes are included in section 5.2 of this Guide

The OJEC is available in electronic format, either in CD-ROM format or by online access to Tenders Electronic Daily (TED) at: <http://ted.eur-op.eu.int/ojs/en/frame.htm>

If the value exceeds the thresholds there are three notices that must be considered.

- **Prior information notice (PIN)**

This is an annual notice to alert prospective bidders as to the availability of forthcoming potential contracts. This notice should be sent for publication in OJEC as soon as the decision is made to go ahead with the procurement.

- **Contract notice**

These are the advertisements that are published in OJEC and tell interested parties how to bid for that contract.

- **Contract award notice**

The contract award notice is sent on completion of the tendering exercise and on award of the contract.

National advertising requirements

The EC public procurement regime is only one of a number of regulatory regimes to which UK authorities are subject. Other national legislation may be applicable.

Option appraisal and the business case for energy services

Overview

3

Key objectives

Appraising the options that will satisfy energy development requirements

Evaluating the outline business case for energy services

Having identified the strategic requirement for energy services development, it will be possible to define a reference project to fulfil this objective. It is then necessary to establish the potential procurement options to meet the service needs described by the reference project. The options might, for example, include:

- maintaining a repair and patch-up operation (commonly described as a 'do nothing' or 'do minimum' option)
- outsourcing energy management and maintenance
- funding energy services development from the capital budget
- seeking a DBFO ESC or similar ESC involving private sector provision.

The options must be carefully appraised in order to understand the costs and benefits of each and to select the option offering best value for money. The range of available options can be established through soft testing of the market, ie discussion with the ESCOs regarding possible solutions.

The option appraisal is a mechanism through which projects of differing investment and complexity can be compared and best value understood.

In order to consider the relative financial benefit of each option and, most importantly, to establish the affordability of each option, it is necessary to determine the life-cycle costs. Each option will have a range of benefits and costs. These must be individually assessed and valued in order to derive a net cash flow. The net cash flows may be discounted over the project life to determine a net present value (NPV) for each option. The project with the highest NPV, or at least net present cost, would normally represent the best value option.

If the case for capital investment is supported by the options appraisal, and third party investment appears to offer a cost-effective means of procurement, the PPP/PFI route should be developed further with the preparation of an outline business case (OBC).

The purpose of the OBC is to ensure that a worthwhile project exists, which has been properly specified and is affordable.

Higher Education
Council Funding for
England – 'Appraising
Investment Decisions'

Treasury publication
– 'The Green Book –
Appraisal and
Evaluation in Central
Government' (HM
Treasury, Second
Edition 1997)

The OBC will be based on the outcome of the options appraisal of the various procurement solutions for the reference project. The OBC requires that the reference project be worked up in sufficient detail to provide full and adequate costing. This will include the quantification of risks.

As procurement is progressed, the business case will evolve and be developed to a detailed business case, setting project budgets, prior to going to formal competition. At all procurement stages it will be necessary to demonstrate and confirm that value for money can be achieved. Reliance on market competition is insufficient and, for most ESCs, value for money must be demonstrated by means of comparison with a conventional public sector solution (a public sector comparator). This will be a model version of the reference project delivered with conventional funding. This will form the budget for the project, against which bids will be measured.

The method for project appraisal and the preparation of a business case for the public sector are addressed in 'The Green Book' and other sector guidance. For PFI projects, a fully developed business case must be produced and, again, 'The Green Book' provides the relevant guidance.

Key issues

- 3.1 Establishing ESC options
- 3.2 The reference project
- 3.3 Assessing the value of services and risk transfer under an ESC
- 3.4 Preparing a business case for energy services
- 3.5 The public sector comparator and determining value for money

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3.1 Establishing ESC options

The range of energy services products, and the capability of the ESCOs, is considerable. To identify potential energy services options, and consider these as part of an option appraisal, it is important for procurers to hold preliminary discussions with the ESCOs.

To benefit from these discussions, it is necessary for the organisation to have established the reference project and to have made a provisional assessment of:

- the acceptable size and length of contract
- the structure of the contract
- the scope for risk transfer
- the employment issues
- the scope for the ESCO to generate income from third parties.

The ESCO will then be able to offer its solutions to the requirements. These may then be incorporated in the appraisal with the knowledge that a practical and available course is being followed from the outset.

3.2 The reference project

Further information can be obtained from: Treasury Taskforce Private Finance Technical Note 5 – 'How to Construct a Public Sector Comparator'

A reference project is a potential solution to the energy development and services need. The purpose of the reference project is to demonstrate technical and financial viability.

The reference project forms the basis of the OBC and public sector comparator (PSC) and may be a combination of capital investments, operations, maintenance and ancillary services, that clearly defines the procurement need.

To define the procurement need and consider the benefits to be afforded by the proposals, it will be necessary to gather information relating to the existing operation. This will include the following.

Energy consumption data

Historic energy consumption data will be required both to assist with the generation of reference project solutions, and to provide a reference against which the solutions may be measured. Latterly detailed energy consumption data and forecasts will be required to develop the PSC and will form the basis of future bid negotiation. It will be necessary to establish:

- existing energy services provisions
- existing consumption
- energy performance
- demand patterns
- predictions for the energy demands of new developments.

As much data as possible should be gathered at the earliest stage to ensure that:

- all strategies and solutions can be fully and effectively priced
- if selected, the ESC route can progress quickly.

Energy consumption data should be readily available from fuel and power invoices. It will be useful to analyse records for several years to ensure that the data is representative of typical energy use.

All fuel and power consumption data should normally be recorded on a monthly basis. Information relating to load factors and heat and power maximum demands should also be obtained where possible.

It will be desirable to incorporate energy performance targets in an ESC. The information collected above may be used to generate performance indices for the existing facilities, and may be adjusted to reflect performance improvements offered by the ESC.

In the case of commercial or residential properties, for example, the performance indices have often been calculated in terms of:

- kWh electrical power per unit floor area – kWh/m²
- kWh fuel per unit floor area – kWh/m².

However, the primary energy consumption of a site is representative of the total resource expended in meeting that site's energy demands. It includes not only the metered consumption of fossil fuel or electricity delivered to the site but also the power station losses incurred in generating the electricity.

A single performance index based on primary energy is therefore usually more appropriate than the above two indices:

- kWh of primary energy per unit floor area – kWh/m².

The use of performance indicators based on primary energy rather than purchased energy is suggested because it more accurately reflects the environmental impact of energy use. This will be particularly useful when considering the merits of displacing purchased electricity with fossil fuel, eg as in the case of a combined heat and power (CHP) scheme.

Adopting this methodology thus means that there will be a closer relationship between performance targets and carbon emissions.

The primary energy consumption of a site may be calculated as follows:

- 1 Multiply the site's purchased electricity consumption (kWh) by the factor 2.9.
This gives an indication of how much fossil fuel would have been consumed in generating the electricity by traditional means.
- 2 Add this value to the site's fossil fuel consumption (kWh).

Maintenance and operational requirements

The reference project will necessarily have to address the requirements for future operations and maintenance. Establishing the cost of existing arrangements enables the benefit of alternative service offerings to be measured.

The organisation should collate and review the:

- relevant historical maintenance records
- operational logs
- staffing requirements.

3.3 Assessing the value of services and risk transfer under an ESC

If an option appraisal is to provide a meaningful indication of value for money, it is important that it should reflect all costs, benefits and risks associated with each option. This will require that each cash flow projection will, wherever possible, include a monetary value for the less tangible items, in addition to the readily identifiable revenues.

Clearly it will not always be possible to quantify benefits and risks in monetary terms, and in these circumstances qualitative judgements will have to be made. This will be particularly important where the choice of preferred options is not clear-cut (ie the NPVs of the various options are similar in value).

In practice, it will be found that many apparently intangible aspects of a service can have a value attached even though there is no market value that could be realised in cash terms.

Risk

Risk is the product of the probability of an event occurring and its financial impact. For instance, if late completion of a new energy plant will result in a consequential loss, then the effect can be expressed in financial terms and added to the appraisal cash flows at the point where the loss would impact. The analysis will depend on having sufficient data to estimate the probability of this event occurring. Such information may be available from the organisation's experience of similar projects or published sources.

Benefit

There may be benefits which, at first sight, appear to be intangible. However, in most cases it should be possible to derive a value. For instance, the installation of a new plant may free up space that could be utilised for other activities. The value in this instance might be considered as the rental or development cost for the new building that would otherwise be required.

3.4 Preparing a business case for energy services

The business case demonstrates the financial benefits, affordability and value for money of the project. As described earlier in this section, the production of an outline business case and subsequent development will demand management time and expertise. It may be beneficial to utilise expert external help, for example:

- engage an independent expert and obtain a full feasibility study
- engage an ESCO that may be a potential contractor to give a full feasibility study
- learn what is available from the market, by discussing all your options with several potential contractors
- Treasury specialists and, for local government, the Public Private Partnerships Programme (4Ps), may assist organisations to construct projects by sharing experience drawn from across the public sector.

The business case will typically address the following issues:

- the strategic benefits of energy services
- an appraisal of the financial benefits
- a quantification and valuation of risk
- an assessment of the affordability
- an output specification clearly defining what is being sought by way of service delivery
- the reference project
- project management – including the project team, timetable and external advisers
- stakeholder support
- for local government, an estimate of the amount of PFI credit sought, if government support for the project is required
- staffing issues.

3.5 The public sector comparator and determining value for money

Further information can be obtained from: Treasury Taskforce Private Finance Technical Note 5 – 'How to Construct a Public Sector Comparator'

In confirming value for money and the validity of a PFI solution, a full business case will need to be developed from the OBC. This is normally completed prior to contract close when final agreed figures are available. The full business case is necessary for local government projects requiring PFI credits because it provides the final calculation for the credit

In order to establish that value for money is being achieved it will be necessary to compare the financial costs/benefits of any proposed DBFO project with those of a conventionally delivered public sector solution. This public sector solution is known as the public sector comparator (PSC), and assumes that all funding requirements are met by conventional public sector means.

An ESC will offer the opportunity to transfer risk from the public sector. It may also provide an operational flexibility, which may be hard to directly translate and model in the PSC. In order to generate a full risk-adjusted PSC it is important that as many of the associated risks and benefits as possible are valued and accounted for in the PSC.

Disclosure of the PSC may assist bid development. PPP/PFI procurement should fall into the negotiated category. Proper communication and information sharing with the private sector bidders is required. Where competition is strong it will be beneficial to disclose the PSC to the bidders. This will enable further refinement. Where there is less competition it may not be appropriate to disclose the PSC, as this could discourage innovation, added value and the provision of the best value for money.

The PSC should be continuously developed to the point at which any further changes would make no significant difference to the outcome of comparison with the intended PPP/PFI solution.

The PSC, suitably developed, will serve to demonstrate value for money at all procurement stages, including the post-negotiation phase of PPP/PFI procurement where final confirmation of value for money can be assessed in the full business case.

Output specifications

Key objective

Developing an energy services output specification

If an ESC is to offer best value for money it will usually be desirable to draw on the skill and expert knowledge of ESCOs for the innovation necessary to arrive at the best solution. Under these circumstances it is preferable to specify the required service needs rather than be prescriptive as to the means of achievement. Such a specification of required service needs is known as an output specification. An output specification will be both functional and performance related.

Functional

Those elements of the specification which define the service to be provided. In the simplest form, this might be the provision of heat and electrical power.

Performance

Those elements of the specification which define a level of performance to be achieved. In the simplest form, this might define electrical capacity and availability obligations.

In the context of ESCs, this type of specification is useful for several reasons:

- it enables bidders to offer alternative and innovative solutions, and thus improves the potential to obtain value for money
- it removes any bias toward a particular solution
- less management time is involved in the preparation of a specification
- the focus is on results and performance.

The specification should give ESCOs enough information to fully assess:

- the scope of the service they are to provide
- whether they are able to provide the service
- a realistic cost for the provision of the defined services.

It is important to understand:

- the information that needs to be assembled and included to allow a proper ESCO response
- the resources and benchmark information that are available to assist in the definition of performance.

Key issues

4.1 The output specification

4.2 Specific considerations

4.3 Energy consumption data and performance benchmarking

4.1 The output specification

The output specification is very different to the traditional prescriptive method of detailed and technical specification. The specification may, however, still include prescriptive elements when they are valid and useful. The output specification usually defines a need in terms of both function and performance.

The specification may be used to define the various levels of required function and performance, as described in the following example.

Specification for the supply of heat and electric power

The contractor will undertake to provide and maintain the supply of steam and electrical power for the purposes of heating, lighting and small power to accommodation wings A, B and C.

Additionally, the specification will define performance requirements, which allow an ESCO to understand its obligations in respect of supplying this heat and power.

For example, these could be as follows.

To make available a minimum supply of 2000 kg/h of steam with 90% availability and at a pressure of 10 barg at a specified metering point. This might be further qualified with tolerance limits defining the maximum acceptable duration of downtime and the minimum and maximum limitations of supply pressure:

- *maximum and minimum hourly demand (kg/h)*
- *condition and quality of steam (dryness fraction)*
- *availability at all times or specific times (% or hours)*
- *maximum allowable downtime (hours or minutes)*
- *maximum and minimum supply pressures (barg).*

Under some circumstances, this limited specification may be satisfactory. If, however, the ESC is to demonstrate improved value for money, when compared to conventional procurement, it will probably be appropriate to transfer more of the operational risk to the ESCO. As discussed earlier in the Guide (see section 2.3), risks should be borne by the party best able to manage them and at least cost. The ESCO may be better placed, because of expert experience and knowledge, to manage energy supply and provide active energy management control. The contractor could, therefore, control energy use while meeting energy and environmental performance targets.

The specification may, therefore, include a further refinement of energy and environmental performance targets to be achieved under contract, for example:

- space temperature – °C
- humidity – %RH
- lighting – lux
- air quality – ventilation rates
- specific energy performance – kWh/m² (the use of primary energy rather than purchased energy is suggested, see section 3.2).

Once an outline output specification has been developed it is important to talk to a number of suppliers. They will be able to offer commercial and technical advice and should be able to provide more information on proposals and suggest improvements. If a sufficient number of companies is not yet known, then consideration should be given to the placement of a PIN.

External consultants will be able to advise on the technical and commercial aspects of the specification. The early stages of developing a contract require a thorough understanding of the objectives and considerations that apply to a specific site.

4.2 Specific considerations

All potential factors must be addressed when developing the output specification. A full assessment of risk and risk transfer will be addressed as the project is developed. Particularly important considerations may include the following.

4.2.1 Outsourcing

Issue

Contracts already in operation may limit the services an ESCO can offer, or influence the way it operates.

Action

All relationships with contractors must be given special consideration. You should include in your contract the ability to change and develop (without making things too difficult or costly) and to resolve any conflicts. Existing service contracts might include:

- fuel purchase
- plant operation
- plant maintenance
- energy management
- system design
- finance
- environmental management
- buildings maintenance
- information technology
- cleaning
- catering
- telecommunications.

4.2.2 New build or major refurbishment

Issue

If the ESC is to be let as part of a new build or major refurbishment project, for which the ESCO is not the main contractor, then care must be taken not to cause conflict with the main contractor.

Action

The programme management risks and communications in relation to works associated with the ESC should, where possible, be passed to the main contractor.

4.2.3 Landlord/tenant agreements

Issue

If the building is leased from a private landlord, there could be contractual difficulties if the ESCO wishes to install and own plant or machinery as part of the arrangement. If the lease is a full repair and maintenance type, then the landlord would not wish to assume any of the liabilities associated with, for example, a sub-let plant room and its contents. There are also legal implications to be addressed in respect of whether equipment installed as part of the ESC becomes fixtures and fittings, ownership of the equipment generally and compensation at the end of the lease. This has implications for PPPs in private-landlord-owned buildings, where ownership would have been an obvious way of transferring risk.

Action

In light of the complicated legal difficulty, advice should be obtained as soon as possible. The risk problems can only be resolved by negotiation with the landlord. These negotiations should be started as early as possible. The government is separately discussing these issues as a general policy matter with Property Advisers to the Civil Estate (PACE).

4.2.4 Lack of management information

Issue

If there is a lack of historical information about energy consumption levels and profiles, then establishing a basis for specifications will be difficult.

Action

You may need to obtain or buy data from your utility company. Another option could be to install more sub-meters to create a database of information before talking to an ESCO.

4.2.5 Timescales

Issue

Any pressing time considerations (such as urgent plant replacement) or limitations on contract length (such as existing leases and contracts) must be taken into consideration. Whenever possible, it is best to avoid placing restrictions on the contract length. Reductions in contract length will inevitably increase ESC charges if the ESCO is still to make an adequate return on its investment.

Action

The timescale, when agreed, should be acceptable to both parties in terms of risk and reward.

4.2.6 Energy and environmental targets

Issue

The public sector has to comply with environmental performance and energy savings targets. Imposed targets are an opportunity to assess and improve performance. Care must be taken to ensure requirements remain realistic in order to control cost.

Action

A well-thought-out and planned approach to specification is required. If high standards of performance are specified, then more expensive equipment may be required. The contractor could assist in reaching any target, but may want longer contract periods to do it.

4.2.7 Legislation

Issue

Legislation and regulations that are or about to become operative (eg planning and environmental regulations) may have an impact. They should be anticipated when considering the output specification.

Action

Contractors must comply with current and future legislation that applies to their activities. The cost of compliance with current and known impending legislation should be borne by the contractor. The cost of compliance with future legislation should be addressed in the contract and risk borne by the party most able to manage the risk.

4.2.8 Maintenance backlog

Issue

Plant often needs maintenance due to prior neglect.

Action

This will need to be taken into account during negotiation with potential contractors so that appropriate valuations can be made.

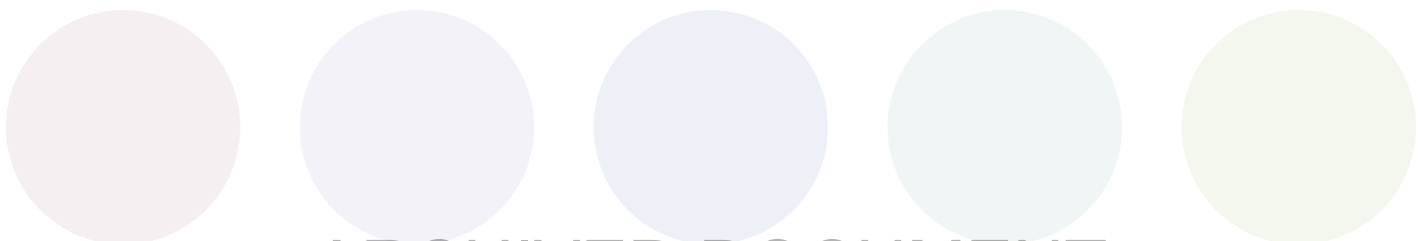
4.2.9 Future operational plans

Issue

Future reorganisations may have a significant impact on the services required, for example, part of the site may close down.

Action

It is vital that all available information be obtained and analysed. Uncertainty regarding what is needed in the future may restrict the scope for investment by an ESCO because of the risk involved. Contracts of more limited scope and shorter duration may be more suitable.



4.3 Energy consumption data and performance benchmarking

It is essential to collate and analyse the existing and projected energy consumption, demand and performance data in order to cost and consider alternative strategies during the options appraisal and to produce a clear output specification.

Comprehensive energy data should be collated as early as possible. The level of information available will determine the quality and suitability of proposals and will reduce the time required developing, refining and selecting proposals for ongoing negotiations.

Historical energy and environmental performance will be the basis for defining and setting performance targets. The contract may incorporate energy or environmental performance targets or a combination of these, eg kWh/m² heated area.

Performance criteria can be useful for setting guidelines and to improve understanding of contract requirements. However, care must be taken to prevent a specification that is too restrictive or impractical.

The criteria and performance will vary with the age, type and condition of the building. As an example, the annual heating requirement per unit floor area for older sheltered housing stock will be considerably greater than the equivalent requirement for a modern intermittently used office building.

The procurer should be aware of any mandatory energy or environmental targets that apply. The output specification should identify the required energy and/or environmental objectives.

These performance criteria must be based on:

- the analysis of current performance from current and historical energy consumption records
- typical or benchmark performance indicators derived from industry guidelines.

For example, these may be expressed as:

- kWh electrical power per unit floor area – kWh/m²
- kWh fuel per unit floor area – kWh/m²
or more appropriately:
- kWh of primary energy per unit floor area – kWh/m².

Researched benchmark information for typical building performance is available from the Energy Consumption Guides produced as part of the Government's Energy Efficiency Best Practice programme (EEBPP), which deal principally with building-related energy consumption and environmental performance in the various sectors. The publications are available from BRECSU Enquiries Bureau (see 'Useful publications' for contact details).

The following tables give details of typical primary energy benchmark information for various building sectors. Using CHP can offer a way of achieving the good practice targets, and indeed surpassing them.

How to calculate primary energy performance indicators.

- 1 Multiply the site's purchased electricity consumption (in kWh) by the factor 2.9. This gives an indication of how much fossil fuel would have been consumed in generating the electricity by traditional means.
- 2 Add this value to the site's fossil fuel consumption (in kWh).
- 3 Divide this sum by the heated floor area.

Building type	Primary energy performance kWh/m ²		
	Good	Fair	Poor
Leisure centres			
Without a pool	< 433	433 - 572	> 572
With a pool	< 795	795 - 1135	> 1135
Pool only	< 1254	1254 - 1802	> 1802
Residential homes	< 375	375 - 646	> 646
Libraries	< 295	295 - 413	> 413
Museums and art galleries	< 391	391 - 548	> 548
Prisons	< 778	778 - 975	> 975
Police stations	< 426	426 - 584	> 584
Fire stations	< 545	545 - 772	> 772
Ambulance stations	< 495	495 - 663	> 663
Crown and county courts	< 455	455 - 612	> 612
Post offices	< 271	271 - 413	> 413
Banks and building societies	< 273	273 - 390	> 390
Restaurants with bar	< 2985	2985 - 3367	> 3367
Fast-food restaurants	< 2858	2858 - 3251	> 3251
Theatres	< 942	942 - 1413	> 1413
Cinemas	< 907	907 - 1084	> 1084
Social clubs	< 314	314 - 569	> 569

Building type	Primary energy performance GJ/100 cu.m	
	Good practice	Typical
Hospitals		
Teaching	73	95
Acute	79	102
Cottage	75	89
Long stay	67	90

Building type	Primary energy performance kWh/m ²	
	Good practice	Typical
Office buildings		
Naturally ventilated cellular	< 175	308
Naturally ventilated open plan	< 236	398
Air-conditioned standard	< 468	833
Air-conditioned prestige	< 793	1248

	Good practice	Typical
Schools		
Primary	< 184	254
Secondary	< 206	261

Building type		
Higher education		
Space type	% of average higher education on campus	Primary energy target kWh/m ²
Teaching	25	215
Research	20	455
Lecture hall	5	725
Office	30	199
Library	10	295
Catering	2.5	2985
Reception	7.5	795
Total academic	100% of academic (75% of total)	403
Total residential	100% of residential (25% of total)	487

Building type	Primary energy performance kWh/m ²		
	Good	Fair	Poor
Industrial buildings			
General manufacturing	< 270	414	> 572
Factory – office	< 260	359	> 515
Light manufacturing	< 180	300	> 503
Storage and distribution	< 138	219	> 310

Additional related information will be necessary for the ESCO to understand the full scope of the contract, assess the potential for operational transfers and to cost the various elements of service provision. These will include, but are not limited to, the following.

A description of the estate

It will be necessary to provide a description of the site or elements of a site to which the contract will apply. For each building this should include details of location, age, construction, usage pattern and ownership.

An inventory of energy-consuming plant

This information may not be necessary for the initial business plan. However, it will assist in the definition of contract needs and should be collected and organised for later use.

For example, list the plant and equipment used for:

- heating
- domestic hot water
- lighting
- air-conditioning
- refrigeration.

Plant and equipment should be identified and as much information as possible about it should be assembled, eg the make, model, age, condition, load factor and efficiency.

Overview Public sector procurement procedures

5

Key objective

Understanding the relevant procurement processes

The procurement rules are defined in detail in the Government's publication – 'HM Treasury Central Unit on Procurement (CUP) Guidance Note No. 51' (July 1995)

Advice on environmental issues for purchasing can be found in the Joint Treasury/DETR note on 'Environmental Issues in Purchasing'

The decision to procure an ESC as a PPP/PFI or traditional procurement will have been determined at the option appraisal. Regardless of the required route, it will be necessary to follow defined procurement procedures, as described below.

Each public sector organisation will have its own procurement procedures based on EC and UK procurement rules. All public sector procurements must follow EC Procurement Directives and the UK regulations that implement them where relevant. The procurement strategies should cover the organisations policies on the environment and procurement.

The issues addressed are as follows:

- advertising in the OJEC
- the criteria for selection of bidders
- the various ways in which interaction with bidders is allowed
- the criteria for contract award.

There are three possible contract award procedures by which a public sector organisation may commission an ESC. These are:

- the open procedure
- the restricted procedure
- the negotiated procedure.

All three are regulated in a different manner.

A free choice is permitted between the open and restricted procedures, but the use of the negotiated procedure is not normally permitted, and can only be used in exceptional and strictly regulated circumstances.

The negotiated procedure can, however, be used for most forms of PPP/PFI procurement, and thus will be applicable to most ESCs.

All three forms of contract award procedure will involve a process of selecting from those who express an interest in performing the work.

In the open procedure, the selection and award stages take place simultaneously. In the case of the restricted and negotiated procedures, these two stages are separated by a legally imposed time period and only those parties who have been formally selected are invited to submit a tender.

Open procedure

Under the open procedure, all interested contractors can tender directly in response to the relevant notice in OJEC. Issues of selection and evaluation are dealt with on receipt of the priced bid that is submitted in response to the advertisement.

No negotiations are permitted in respect of the bids submitted, which are evaluated on the basis of pre-published award criteria.

This procedure is rarely utilised in the UK by virtue of the number of responses that might have to be evaluated.

This procedure is not suitable for PFI projects and has very limited potential in the context of ESCs and it thus is not considered further here.

Restricted procedure

The restricted procedure is the most common procedure used in the UK, outside PFI procurement. Those to be invited to tender can be selected from those that respond to the advertisement. Those potential tenderers are then asked to respond directly to an invitation to tender. The scope for negotiation is strictly limited, and tenders are evaluated on pre-published award criteria.

This procedure is the most relevant for the traditional procurement method. It is not recommended for PPP/PFI projects, but where the negotiated procedure cannot be justified, it may have to be utilised.

Negotiated procedure

Under this procedure, the selection stage is broadly the same as for the restricted procedure, but after that, the contracting authority is only required to issue invitations to negotiate to those it selects.

This procedure can only be used in very limited circumstances defined by legislation. The negotiated procedure is the most appropriate form of procurement for PPP/PFI projects and will usually apply to ESCs.

Key issues

- 5.1 The nature of the procurement – mixed contracts
- 5.2 Advertising in the OJEC
- 5.3 The criteria for selection of bidders
- 5.4 The various ways in which interaction with bidders is allowed
- 5.5 The criteria for contract award
- 5.6 Post-contract award

5.1 The nature of the procurement – mixed contracts

The first task is to determine precisely what is being purchased, that is whether it falls within the definition of works, supplies or services. All procurements fit within one of these categories and UK regulations for contracting authorities are different for each, although sharing a common set of principles. It is in the context of the negotiated procedure that one of the main differences is found, in that the rules for supplies are not as favourable as for works, and in turn, those rules are not as favourable as for services.

It is the nature of PFI and most ESCs that payment is made for a service. Nevertheless, the issue of mixed contracts arises in a number of situations, perhaps the most common being the overlap of supplies and services and the overlap of works and services.

The problem of categorising mixed contracts is set out in guidance produced by the Central Unit on Procurement of the Office of Government Commerce (CUP Guidance Note 51).

This states as follows:

In most cases the classification of contracts will be straightforward. The regulations provide that where a contract covers both services and supplies, including any siting and installation of the goods, the classification should be determined by the respective values of the two elements. Where a contract provides for the supply of equipment and an operator it should be regarded as a services contract. Contracts for software are considered to be for services if bespoke, supplies if off the shelf, except that contracts placed by utilities for telecommunications software are for supplies.

There is, however, no value based formula for determining into which category a mixed works/supplies or works/services contract falls. In such cases, the contracts should be classified according to its predominant purpose.

5.2 Advertising in the OJEC

The OJEC is available in electronic format either in CD-ROM format or by online access to Tenders Electronic Daily (TED) at: <http://ted.eur-op.eu.int/ojs/en/frame.htm>

It will be necessary to observe EU rules on the procurement of assets and services. The EC Public Procurement regime regulates the manner in which contracting authorities may enter into contracts for the procurement of works, supplies, and services. It requires regulated tendering within strict timetable constraints, preceded by formal advertisement throughout the EC. In the context of ESCs, EU rules require that all projects, exceeding published threshold values, be advertised in the OJEC.

THRESHOLDS – PUBLIC SECTOR: 1 JANUARY 2000 TO 31 DECEMBER 2001

The current thresholds can be obtained from: HM Treasury's website: <http://www.hm-treasury.gov.uk>

	Supplies	Services	Works
Entities listed in Schedule 1 (S.I. 1995/201) ¹	£93 896 (SDR130 000) ⁴ (Euro 139 312)	£93 896 ² (SDR130 000) (Euro 139 312)	£3 611 395 ³ (SDR5 000 000) (Euro 5 358 153)
Other public sector contracting authorities	£144 456 (SDR200 000) (Euro 214 326)	£144 456 ² (SDR200 000) (Euro 214 326)	£3 611 395 ³ (SDR5 000 000) (Euro 5 358 153)
Indicative notices	£505 500 (Euro 750 000)	£505 500 (Euro 750 000)	£3 611 395 (Euro 5 358 153)
Small lots	Not applicable	£53 920 (Euro 80 000)	£674 000 (Euro 1 000 000)

Notes to table

- Schedule 1 of the Public Supply Contracts Regulations 1995 lists central government bodies subject to the WTO GPA. These thresholds will also apply to any successor bodies.
- Certain services have a threshold of £134 800 (Euro 200 000) and these are detailed on HM Treasury's website.
- For subsidised works contracts under regulation 23 of the Public Works Contracts Regulations 1991 the threshold is £3 370 000 (Euro 5 000 000).
- The SDR (Special Drawing Right) is an artificial currency, based on a basket of five currencies, used by the IMF (International Monetary Fund) as its unit of account and used for IMF transactions and operations.

If the value of the ESC is below the EC thresholds, the public sector must comply with general EC duties not to favour national or local suppliers.

If the value is above the EC thresholds, there are three notices that may be required:

- prior information notice (PIN)
- contract notice
- contract award notice.

ARCHIVED DOCUMENT

Transparency is one of the key principles of the EC regime. Consequently, there is a requirement under all procedures (including the negotiated procedure, except in very limited situations) for the prior publication of notices or advertisements.

The format of the notices varies slightly depending on whether the procurement is of works, supplies or services.

All notices and communications should be sent to:

Office for Official Publications of the European Communities (EUR-OP)

2 Rue Mercier

L-2985 Luxembourg

Tel 00 352 29 29 42 455

Fax 00 352 29 29 42 670 or 00 352 29 29 44 623

Prior information notice (PIN)

This notice should be sent for publication in OJEC as soon as the decision is made to go ahead with the procurement. The purpose of this notice is to alert prospective bidders as to the availability of forthcoming potential contracts. Following the publication of a PIN, at least 52 days (and not more than one year) must elapse before any contract notice is posted.

- The PIN only includes essential project characteristics.
- The PIN is not an optional notice. The rules specifically make this mandatory where the relevant threshold is triggered.

Contract notice

Contract notices must be sent to OJEC, allowing not less than 37 days from despatch (or 15 days in cases of genuine urgency), for requests to be selected to tender. After invitations to tender have been issued, a minimum of 40 days, or 26 where a PIN has been published (or 10 days in cases of urgency), should be allowed for receipt of tenders.

- These advertisements inform interested parties how to bid for a contract.
- They include substantial detail on the nature of the contract to be awarded and the manner in which interested parties must respond to the notice. The format varies depending on the contract award procedure utilised.

Contract award notice

A contract award notice should be sent to OJEC no later than 48 days after a contract has been awarded.

- The contract award notice is sent on completion of the tendering exercise upon award of the contract.
- The format of the notice is laid down in the relevant legislative provisions.
- If the contract is abandoned and there is no award, the EC must be notified by letter. No particular format is required for the notice of abandonment, but reference should be made to the original contract notice, stating when the procedure was abandoned.
- Every tendering exercise that is originally advertised in OJEC should be completed with a contract award notice or notification of abandonment.

Drafting the notices

Drafting in accordance with the model forms of notice laid down in the relevant statutory instrument can sometimes prove to be difficult. Advertisement proforma are available at HM Stationery Office, and are also available on the Internet at <http://ted.eur-op.eu.int/ojs/en/frame.htm>. However, a general explanation of the different sub-headings within the model forms is set out below. A typical contract notice may look something like the following.

Award procedure/contract type	Negotiated service
1 Awarding authority	Anyplace City Council (address) Tel [] Facsimile []
2 Category of services	Anyplace City Council is reviewing its energy provision arrangements and is seeking expressions of interest from suitably qualified and experienced energy service providers.
CPC reference numbers	[]
3 Delivery to	The Combined City Complex, Anytown.
4 a Reserved to a particular professions	No.
b Law regulation or administrative provision	None.
c Names and professional qualifications of staff	The successful tenderer will have to disclose the names and professional qualifications of the staff who will be responsible for the services. See 12 below.
5 Division into lots	Service providers should indicate whether they could provide some or all of the service.
6 Number of service providers	Not known at this stage, subject to interest likely to be in the range 3 to 5.
7 Variants	Variant bids will be permissible, provided the contracting authority agrees that the core requirements will be met.
8 Duration of contract	To be determined during the negotiation.
9 Legal form in the case of group bidders	No special legal form but group bidders shall be required to be jointly and severally responsible for the contract.
10 a Accelerated time limits	Not applicable.
b Deadline for receipt of applications to participate	(dd/mm/yy)
c Address to which applications should be sent	As in 1 above.
d Language in which applications must be drawn	English.
11 Deposits or guarantees	A performance bond and parent company guarantee may be required.
12 Qualifications	Prospective service providers will be required to complete a prequalification questionnaire detailing the information requirements and other standards required by the City Council.
13 Providers already selected	Not known at this stage, subject to interest.
14 Other information	Prospective service providers will be issued with an information memorandum outlining the Council's current energy provision arrangements and anticipated future needs. The Treasury Taskforce has approved this project for procurement under the PFI. Any visits to the City Complex to inspect the current facilities should be completed by dd/mm/yy. They should be arranged through S. Smith at the address and telephone number above.
15 Date of despatch of notice	(dd/mm/yy)
16 Dates of previous publications in the OJEC	(dd/mm/yy)

Where a negotiated procedure is used for a PPP or PFI ESC, variants will not present any difficulty

Notes on completing OJEC notice form

- 2 **CPC reference number (in services).** This is the Central Product Classification system of the United Nations. This will be replaced by Common Procurement Vocabulary, which has now been published by the EC Commission.
- 5 **Division into lots.** This describes the packages into which the project is subdivided.
- 7 **Variants.** Variants relate to the different manner in which responses to the invitation to tender may be completed. One example would be if there were two different pricing mechanisms that were both acceptable to the contracting authority. In the open and restricted procedures, all negotiations are prohibited. Therefore, no 'back door' negotiations are permitted through the use of variants. Specific rules govern the use of variants.
- 8 **Duration of contract.** Certain permitted extensions to the contract period are only permitted if prior notice has been given in the advertisement.
- 10 **Deadline for receipt of applications.** Depending on the procedure adopted, different time limits apply.
- 12 **Qualifications.** This is one practice that has been developed to ascertain technical/financial criteria. There are, however, limits as to what can be asked. This can be achieved by either listing the requirement in the advert or by asking potential tenderers to complete a questionnaire. But the questionnaire must not ask for more than that permitted. Advice should be sought to determine the most appropriate method.
- 13 **Providers already selected.** If a number is specified, it should be in excess of three.
- 14 **Other information.** This section is very useful for dealing with the context of the tendering exercise. As in the example, a reference to providing an information memorandum outlining requirements should be given. Another example could be when it is required as part of another regulatory regime relating to a practical example in the field of waste management and the overlap with the Environmental Protection Act 1990.

National advertising requirements

The EC public procurement regime is only one of a number of regulatory regimes to which UK authorities are subject. Examples of these are the CCT regime and the regime regulating waste authorities under the Environmental Protection Act 1990. The authority may have to integrate these into the tendering process.

No additional information, to that provided in the OJEC notice, may be given in the UK advertisements, nor may any prior advertisement be published. This would be regarded as discriminatory conduct and prohibited by general EC principles of non-discrimination.

5.3 The criteria for selection of bidders

Having received expressions of interest, it will be necessary to quickly reduce the number of potential bidders to a shortlist. The shortlist should not be less than three bidders, unless the public authority has specified a range (using the restricted procedure) in which the number of participants will fall, in which case the minimum number will be five. This selection process is subject to specific selection rules, criteria and timescales.

5.3.1 Selection criteria

EC and UK rules govern the selection process and the permitted selection criteria. Care must be taken in the drafting of any tendering documentation (eg advertisements, questionnaires and invitations to tender) to avoid any wording or practice which may directly or indirectly favour a UK contractor over one from elsewhere in the EC, or ask for additional information not described in the rules.

The three areas, which may be examined for selection, are as follows.

Selection/rejection factors

These include such matters as bankruptcy, registration on the appropriate professional trade register in the Member State, absence of relevant convictions on the part of the firm contracting and absence of grave misconduct, etc. Any firm that applies for work, and is unable to satisfy these factors, can automatically be rejected.

Economic and financial standing

Each authority can have its own financial 'threshold' or standard that a contracting firm must meet. This standard may include a certain level of turnover or other measure of financial stability. Any firm that fails to meet the standard laid down by the authority, based on evidence stipulated in the relevant legislation, may be rejected.

Technical knowledge and ability

The authority may again set standards of technical knowledge and ability that all contracting parties must meet. The evidence that may be taken into account is governed by EC rules. Here the authority will be exercising some level of judgement based on the presence or absence of various permitted matters, such as qualified staff and relevant past performance, to indicate appropriate experience. Care needs to be taken when assessing the operating capability of a holding company with operating subsidiaries.

Generally, a preferred bidder must have the resources and management skills to undertake the pre-contract negotiations professionally and efficiently and it must be clear that they have the ability to deliver.

5.4 The various ways in which interaction with bidders is allowed

Under most circumstances, the negotiated procedure will be most suitable for the procurement of ESCs offering the prospect of negotiation at all stages of the tendering exercise. The restricted procedure is less appropriate, as only limited post-tender negotiations are permitted, which must not involve discrimination or distort competition.

Posting the contract notice will elicit a response from those wishing to tender. The selection criteria should be applied and the number of prospective tenders reduced to the shortlist as described in section 5.3. Having obtained the shortlist, the bidders will be invited to submit their priced offer in the case of a restricted procedure, or invited to submit an offer following an invitation to negotiate in the case of a negotiated procedure.

In the case of the restricted procedure, the invitation to tender is accompanied by the detailed specification from which the bidder will derive the scale and scope of the service it is to provide, and on which it will base its priced bid. The contract award will subsequently be made as described below.

Negotiations for PPP or PFI projects will normally proceed as follows.

Prequalification of bidders

The list of respondents who have notified their interest on receipt of the information memorandum should be reduced to a shortlist. It is advisable to test bidders against pre-determined criteria to profile suppliers. Once the tests have been completed, they should not be done again.

Shortlist

The shortlist should be devised on the basis of ability and commitment to do the work. There may be a first and then a final list. It is probable that the authority would request some technical response from bidders as to their willingness to take on the risks of the project. Criteria for selection should be in accordance with EU procurement legislation which excludes pricing at this stage. Any bidders who are not selected should be told and debriefed immediately as to what their shortcomings were.

Refining the appraisal/preparing and issuing the Invitation To Negotiate (ITN)

The original appraisal should be looked at again with the advantage of the information and experience gained by this time. The business case and funding arrangements should also be reaffirmed. The bidders should be told that this has been done.

Work on the ITN should begin at the earliest possible stage. This document tells bidders how to submit their bid (BAFO (best and final offer)) and the process which will be used in order to evaluate it. In practice, it should be a further development of the information memorandum.

The following information should be included:

- the service required, expressed as outputs
- any constraints
- the proposed contractual terms – particularly those relating to:
 - performance
 - payment mechanisms
 - and contract length (term)
- the proposed timetable and process for negotiating:
 - an acceptable set of terms and conditions
 - and for submitting bids
- the criterion for evaluating bids
- the extent to which bidders are encouraged to submit variant bids
- financial criteria including:
 - the PSC
 - and affordability constraints.

It is possible to build in a stage whereby you issue a preliminary draft set of ITN documentation and then talk to the selected bidders about it, before issuing it in final form. This can help clarify the process and enables the bidders to commit to the ITN.

Negotiation

Following the issue of the ITN, depending on the number of bidders at this stage, a negotiation process will take place.

Receipt and evaluation of BAFOs

Following receipt of the negotiating positions from bidders, value for money and affordability must be confirmed and the solution offered demonstrated as 'robust', ie likely to work.

The project team should then evaluate the bids in accordance with the pre-published criteria set out in the invitation documentation. Some ranking of bids is usual and negotiations may be conducted in parallel or only with a preferred bidder depending on that ranking and the available resources.

It may be necessary to allow a degree of clarification and negotiation of bids, but key contractual clauses should not be renegotiated at this stage nor should any other aspect of what is being procured change in any material way.

Further information can be obtained from: Treasury Taskforce 'Step-by-Step-Guide to the PFI Procurement Process' (April 1998)

The contract negotiation stage can often prove to be protracted because of lack of clarity at earlier stages, leading to:

- lack of clarity in the ITN documentation
- insufficiently detailed analysis of the bid quality of the preferred bidder.

This stage may conclude with the presentation of a BAFO which can be accepted. At this stage, the project team should have satisfied itself that the proposed bidder is capable of delivering the project. If there is to be any final negotiation stage after BAFO, this should be limited to:

- fixing the final detail of the transaction documentation
- satisfying the reasonable requirements of the ESCO's funders (in the case of ESCOs without internal funding arrangements).

The intention is not to re-open key commercial issues and terms for discussion at this late stage.

5.5 The criteria for contract award

The award should be made on the basis of the pre-determined criteria that applied to the bid/BAFO.

The bid/BAFO should:

- be affordable
- represent an acceptable degree of risk allocation between the procurer and the ESCO
- be the 'most economically advantageous' solution that can be obtained in the circumstances, representing better value for money than the public sector comparator
- be deliverable by the preferred bidder.

Further information can be obtained from: Treasury Taskforce Private Finance Technical Note 4 – 'How to appoint and work with a preferred bidder'

ARCHIVED DOCUMENT

5.6 Post-contract award

A notice of contract award should be published in OJEC.

Unsuccessful bidders have the right to request a debriefing and to know the outcome of the tender.

The EC regime provides remedies for any aggrieved candidates. These ensure the correct application of EC procurement rules. The UK regulations allow proceedings in the High Court (Court of Sessions in Scotland) where a process may be stopped and/or damages awarded. Aggrieved parties can also complain to the EC.

Award of the contract is not, of course, the end of the story. The contract must now be managed, and best practice would suggest that there should be some mechanism to ensure continuity between the procurement team and the contract managers. Often the management of the contract is by a number, if not all, of the procurement team. If this is not the case, then the management team should have had some part to play in the procurement process.

Addresses

BRECSU
BRE
Garston
Watford WD25 9XX
Tel 01923 664258
Fax 01923 664787

CHPA
Combined Heat and Power
Association
Grosvenor Gardens House
35/37 Grosvenor Gardens
London SW1W 0BS
Tel 020 7828 4077
Fax 020 7828 0310

Energy Saving Trust
21 Dartmouth Street
London SW1H 9BP
Tel 020 7222 0101
Fax 020 7654 2444

ESA
Energy Services Association
Grosvenor Gardens House
35/37 Grosvenor Gardens
London SW1W 0BS
Tel 020 7828 4077
Fax 020 7828 0310

ESTA
Energy Systems Trade
Association
PO Box 77
Benfleet SS7 5EX
Tel 07041 492049
Fax 07041 492050

ETSU
AEA Technology plc
Harwell
Didcot
Oxfordshire OX11 0RA
Tel 01235 433302
Fax 01235 432390

Office of Government Commerce
Private Finance Policy Team
2-6 Salisbury Square
London EC4Y 8AE
Tel 020 7270 5527
Fax 020 7389 9739

Local Government Association
35 Great Smith Street
Westminster
London SW1P 3BJ
Tel 020 7664 3000
Fax 020 7664 3030

Public Private Partnerships
Programme (4Ps)
6th Floor
83 Victoria Street
London SW1H 0HW
Tel 020 7472 1550
Fax 020 7472 1560

Partnerships UK
Private Finance Projects Team
10 Great George Street
London SW1P 3AE
Tel 020 7273 8383
Fax 020 7273 8368

Useful publications

HM TREASURY

From HM Treasury's Public Enquiry Unit, HM Treasury, Parliament Street,
London SW1P 3AG

Tel 020 7270 4558/4860/4870. Fax 020 7270 5244

- Step-by-Step Guide to the PFI Procurement Process [Revised April 1998]
(http://www.treasury-projects-taskforce.gov.uk/series_1/step/step0.htm)
- Partnerships for Prosperity – The Private Finance Initiative [November 1997]
(http://www.treasury-projects-taskforce.gov.uk/series_1/contents.htm)
- Writing an Output Specification [October 1996]
(http://www.treasury-projects-taskforce.gov.uk/series_other/writing/writing4.htm)
- Treasury Task force policy statements
- Policy Statement No. 1 – PFI and Public Expenditure Allocations [September 1997]
(http://www.treasury-projects-taskforce.gov.uk/series_2/doct1.htm)
- Policy Statement No. 2 – Public Sector Comparators and Value for Money
[February 1998]
(http://www.treasury-projects-taskforce.gov.uk/series_2/doct2.htm)
- Policy Statement No. 3 – PFI and Public Expenditure Allocations for Non-Departmental
Public Bodies [August 1998]
(http://www.treasury-projects-taskforce.gov.uk/series_2/doct_3/doct3_1.htm)
- Policy Statement No. 4 – Disclosure of Information and Consultation with Staff and
other Interested Parties [October 1998]
(http://www.treasury-projects-taskforce.gov.uk/series_2/doct_4/doct4_1.htm)
- Technical Note No. 1 (Revised) – How to Account for PFI Transactions [June 1999]
(http://www.treasury-projects-taskforce.gov.uk/series_3/technote/tech_contents.htm)
- Technical Note No. 2 – How to follow EC Procurement Procedure and Advertise in the
OJEC [June 1998]
(http://www.treasury-projects-taskforce.gov.uk/series_3/technote2/2tech_01.htm)
- Technical Note No. 3 – How to Appoint and Manage Advisers to PFI Projects [August 1998]
(http://www.treasury-projects-taskforce.gov.uk/series_3/technote3/3tech_00.htm)
- Technical Note No. 4 – How to Appoint and Work with a Preferred Bidder [July 1999]
(http://www.treasury-projects-taskforce.gov.uk/series_3/technote4/4tech_contents.html)
- Technical Note No. 5 – How to Construct a Public Sector Comparator
(http://www.treasury-projects-taskforce.gov.uk/series_3/technote5/5tech_contents.html)
- HM Treasury and DETR Note on Environmental Issues in Purchasing (April 1999)
(<http://www.hm-treasury.gov.uk/docs/1999/envte2.html>)

Useful publications

CENTRAL GUIDANCE

- Appraisal and Evaluation in Central Government 'The Green Book' 7/1/97
- CUP Guidance No. 30 Specification Writing (supersedes guidance no 9) 6/1/91
- CUP Guidance No. 35 Life Cycle Costing 4/1/92
- CUP Guidance No. 40 The Competitive Tendering Process
- CUP Guidance No. 51 Introduction to the EC Procurement Rules 7/1/95
- CUP Guidance No. 54 Value Management 1/1/96
- CUP Guidance No. 57 Strategic Partnering in Government [is about output specifications] 5/1/97
- Staff transfers in the public sector – Statement of Practice (January 2000).
Published by the Cabinet Office – <http://www.cabinet-office.gov.uk/civilservice/2000/tupe/>
- Financial Reporting Standard 5 (FRS5) Reporting the Substance of Transactions
- SSAP21 Accounting for Leases and Hire Purchase Contracts 30/11/97

EDUCATION AND EMPLOYMENT

From Department for Education and Employment Publications Centre
PO Box 5050, Sudbury, Suffolk CO10 6ZQ. Tel 0845 6022260. Fax 0845 6033360
Website: <http://www.dfee.gov.uk/ppppfi/>

- Public Private Partnerships: A guide for School Governors [January 1999]
- Partnerships in Practice: Case Studies in Further Education [1999]
- Investment Appraisal Guide – Department for Education and Employment 01/02/97
- Practical Guide to PFI for Higher Education Institutions – Department for Education and Employment 01/11

LOCAL GOVERNMENT

- Local Government and the Private Finance Initiative – An explanatory note on PFI and Public/Private Partnerships in local government. [Updated September 1998. Code 98FD0340]
(<http://www.local-regions.detr.gov.uk/pfi/index.htm>)
- A Guide to the Local Government Capital Finance System. [Reprinted September 1998]. Code 97DPL005 (<http://www.local.detr.gov.uk>)

From the Government's Publication Sales Centre

Unit 8, Goldthorpe Industrial Estate, Goldthorpe, Rotherham S63 9BL.
Tel 01709 891318. Fax 01709 881673

- Taking the Initiative, A Framework for Purchasing Under the Private Finance Initiative [September 1998. ISBN 1862401195 Audit Commission Publications freephone 0800 502030]
- Private Finance Initiative – Revenue Support Arrangements for 1998/99: Guidance for Authorities, Version 1 [9 June 1998. Available from LGC, Flr 5/H3 Eland House, Bressenden Place, London SW1E 5DU]

Useful publications

PUBLIC PRIVATE PARTNERSHIP PROGRAMME (4PS) GUIDANCE

From IDA Publication Sales, Layden House, 76-86 Turnmill Street, London EC1M 5LG
Tel 020 7296 6600. Fax 0171 296 6666

**** From the Public Private Partnerships Programme**

6th Floor, 83 Victoria Street, London SW1H 0HW
Tel 020 7472 1550. Fax: 020 7472 1560
Website: <http://www.4ps.co.uk>

- Options Appraisal and the Outline Business Case **
- A Guide to the Local Government (Contracts) Act 1997 – a practical guide to the provisions and their effect. [Ref PFO50 ISBN 1 84049 019 5]¹
- Output Specifications for PFI Projects – A 4Ps guide [1999 Ref PFO58 ISBN1 84049 108 6]¹
- Output Specifications for PFI Projects – A 4Ps guide summary [1999] **

ENERGY EFFICIENCY BEST PRACTICE PROGRAMME PUBLICATIONS

From BRECSU Enquiries Bureau, Garston, Watford WD25 9XX
Tel 01923 664258. Fax 01923 664787. E-mail brecsuenq@bre.co.uk

- Unlocking the potential – financing energy efficiency in private housing (GIR 50)
- Taking stock – private financing of energy efficiency in social housing (GIR 51)
- Guide to community heating and CHP (GPG 234)
- Combined heat and power (CHP) in universities (GPG 204)
- Energy efficiency in sports and recreation buildings: CHP – the 'supplier financed' option (GPCS 281)
- Energy performance in the Government's civil estate (GPG 286)
- Energy use in Ministry of Defence establishments (ECON 75)
- Energy consumption in hospitals (ECON 72)
- Energy use in offices (ECON 19)
- Energy efficiency in further and higher education (ECON 54)
- Energy efficiency in sports and recreation buildings (ECON 51)
- Saving energy in schools (ECON 73)

NHS

From Department of Health, Distribution Centre, PO Box 777, London SE1 6XH
Fax 01623 724524

- CAPITAL INVESTMENT MANUAL – Private Finance Guide – NHS Executive
Health 01/01/94
- HEALTH SERVICE GUIDELINES – Private Finance and Capital Investment Projects –
NHS Executive HSG(95)15
Health 20/03

Glossary of terms

BAFO	This is a frequently used term (not covered in the regulations) to describe best and final offer (negotiated procedure)
BOOT	Build, own, operate and transfer ownership at the end of a contract. A contract type
BOP	Build, operate and partnership manage. A contract type
CUP	Central unit on procurement. HM Treasury Department, which gives advice on procurement
DBFO	Design, build finance and operate. A contract type
EEBPp	Energy Efficiency Best Practice programme. A government programme promoting energy efficiency in the UK
ESC	Energy services contract
ESCO	Energy services company
FM	Facilities management
FRS5	Financial Reporting Standard 5 'Reporting the Substance of Transactions'
Negotiated procedure	A procurement procedure used when the specification can only be developed by negotiation with bidders
NPV	Net present value
OBC	Outline business case
OJEC	Official Journal of the European Community
Open procedure	A procurement procedure under which any party may submit a tender
PACE	Property Advisers to the Civil Estate – April 1st 1996
PFI	Private Finance Initiative
PIN	Prior information notice
PPP	Public Private Partnership
PSC	Public sector comparator
Restricted procedure	A procurement procedure under which only selected parties may submit tenders
ROL	Rehabilitate, operate and leaseback. A contract type
SDR	Special Drawing Right
SSAP21	Statement of Standard Accounting Practice 21 'Accounting for Leases and Hire Purchase Contracts'
TED	Tenders Electronic Daily – the OJEC on-line tender database
TUPE	Transfer of Undertakings (Protection of Employment) regulations

Energy services
– the business proposition

Energy services
– the strategic issues

Option appraisal and the
business case for energy
services

Output specifications

Public sector
procurement procedures

The Government's Energy Efficiency Best Practice programme provides impartial, authoritative information on energy efficiency techniques and technologies in industry and buildings. This information is disseminated through publications, videos and software, together with seminars, workshops and other events. Publications within the Best Practice programme are shown below.

For further information on:

Buildings-related projects contact:
Enquiries Bureau

BRECSU

BRE

Garston, Watford WD25 9XX

Tel 01923 664258

Fax 01923 664787

E-mail brecsuenq@bre.co.uk

Industrial projects contact:
Energy Efficiency Enquiries Bureau

ETSU

Harwell, Oxfordshire

OX11 0RA

Tel 01235 436747

Fax 01235 433066

E-mail etsuenq@aeat.co.uk

The Government's Energy Efficiency Best Practice programme website can be found at <http://www.energy-efficiency.gov.uk>

Energy Consumption Guides:

compare energy use in specific processes, operations, plant and building types.

Good Practice:

promotes proven energy-efficient techniques through Guides and Case Studies.

New Practice:

monitors first commercial applications of new energy efficiency measures.

Future Practice:

reports on joint R&D ventures into new energy efficiency measures.

General Information:

describes concepts and approaches yet to be fully established as good practice.

Fuel Efficiency Booklets:

give detailed information on specific technologies and techniques.

Introduction to Energy Efficiency:

helps new energy managers understand the use and costs of heating, lighting, etc.

